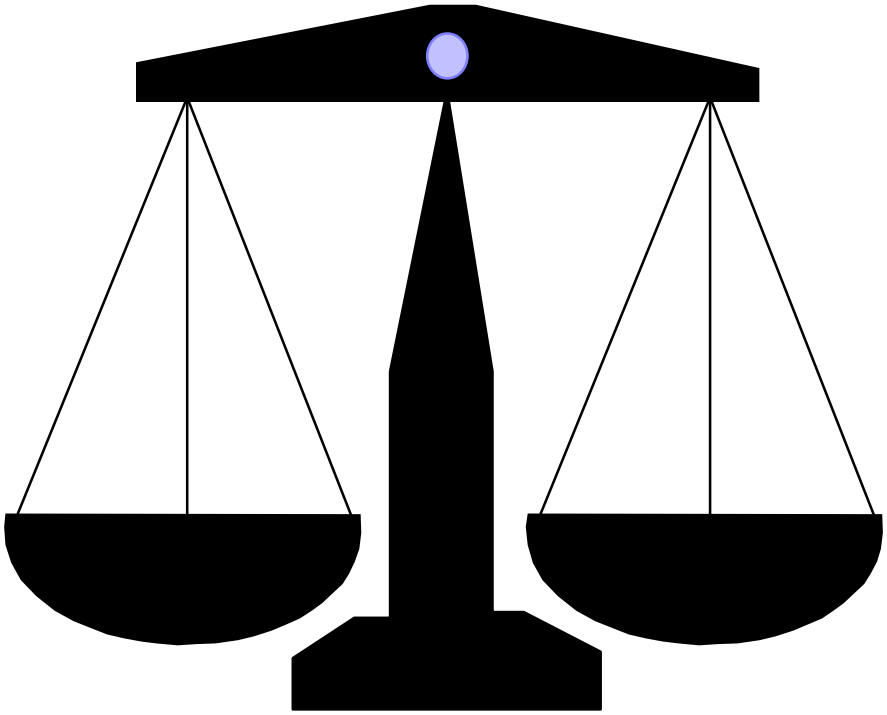
The Enforcement of Arbitration Agreements in Loan Contracts, Pursuant to Indiana Law



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INTRODUCTION

Arbitration agreements used in Indiana must be examined under two substantive standards, state and/or federal law. Indiana law regarding arbitration is provided for in the Uniform Arbitration Act (UAA)[1], which mirrors federal law except for one important aspect. The difference is that Indiana excepts arbitration clauses in consumer loan contracts. Federal law regarding arbitration is provided for in the Federal Arbitration Act (FAA)[2], and contains no such exceptions. Determining whether an arbitration agreement is governed under state or federal jurisdiction is of the utmost importance in any determination regarding its enforceability.

The question of whether a binding arbitration agreement used in a consumer loan contract is enforceable is ultimately fact-sensitive. It must first be determined whether federal or state law applies in a particular case. If federal law applies, an arbitration agreement can only be challenged by a borrower under general contract principles of that state such as unconscionability, fraud, or duress. Federal law ***does not apply*** if the transaction is purely ***intrastate***, and not interstate, commerce. In addition, federal law might not apply if the parties to the contract have chosen to bind themselves under a particular state's laws.

Indiana law calls for the enforcement of arbitration agreements in all contracts except for consumer leases, sales, and loan contracts.[3] This exception has been created to protect consumers who may be uneducated and unfamiliar with financial matters. While this is a well-intentioned reason, it is not enough to defeat the federal presumption in favor of enforcing arbitration agreements. Federal law favors the enforcement of all arbitration agreements, regardless of the type of transaction, and will preempt state law under the U.S. Constitution's Supremacy Clause[4] if the contract involves interstate commerce.

First and foremost, it is necessary to determine whether or not the FAA applies to an arbitration clause. The United States Supreme Court has held that any arbitration agreement affecting interstate commerce is

[1] IAC 34-57-2-1.
[2] 9 U.S.C.A. §1 et seq.
[3] IAC 34-57-2-1. Written agreement to arbitrate; enforceability; exemptions from chapter.
[4] U.S.C.A. Const. Art. 6, cl. 2

subject to the FAA. There are four considerations when making this determination:

1. Whether the transaction involves interstate commerce.
2. If so, then the federal act preempts state law under the Supremacy Clause.
3. The only restrictions which may be applied by states in this situation are those that apply to all contracts generally, and not just arbitration clauses; e.g. unconscionability, fraud, or duress.
4. State law will apply if the agreement contains a choice of law clause, which will then be honored as a term agreed to by contract.

Generally speaking, the question of whether or not the parties agreed to arbitrate is a simple one. If an arbitration clause is a part of the contract, and no general contract defense is available, then the clause is enforceable under the FAA if interstate commerce is involved. The federal policy of encouraging arbitration leads to a broad reading of any arbitration clause in order to make it apply. Most importantly, it cannot be challenged under any theory or defense that applies only to arbitration clauses. For example, if the contract involves interstate commerce then Indiana's statute, which specifically excludes enforcement of arbitration clauses in consumer loan contracts, would be preempted by the federal act. This is because arbitration clauses are singled out for treatment different from the treatment of contracts in general.

The law is different if the contract does not involve interstate commerce. A purely intrastate transaction does not fall under the jurisdiction of the FAA. Therefore, an ***intrastate*** transaction would still be subject to the exclusion of arbitration clauses in consumer loan contracts. The initial question then should be whether or not a particular contract is a transaction involving interstate commerce. If so, the FAA preempts state law. If not, the FAA does not apply and state law is controlling.

This means that the review of arbitration clauses is extremely fact-sensitive. The clause's language and the circumstances surrounding it determine whether the clause is binding. The mere statement in the contract that the provisions of the FAA apply is not enough to evidence a transaction involving interstate commerce. There must be minimal contacts crossing state lines in order for

interstate commerce to exist. Furthermore, the party seeking to compel arbitration must establish their right to arbitrate under the FAA.[5] Even if the transaction involves interstate commerce, however, state law might still apply if there is a choice of forum clause in the contract that establishes the applicable law. Different courts have found that state law is not preempted by the FAA where the parties agree that state law will govern their arbitration agreement.[6] All of these determinations must be made before an arbitration clause in a consumer loan contract can be considered either enforceable or unenforceable under Indiana law.

CHOICE OF LAW

United States Supreme Court decisions make it clear that the FAA ensures that an agreement between parties to submit to arbitration will be enforced according to its terms even if state law would otherwise exclude such claims from arbitration. The Court has stated, and reiterated, that "…the FAA not only 'declared a national policy favoring arbitration,' but actually 'withdrew the power of the states to require a judicial forum for the resolution of claims which the contracting parties agreed to resolve by arbitration.'"[7] This does not mean, however, that the FAA prevents parties from creating arbitration terms in their contract separate from the federal Act. The FAA is the governing act in the event that no other terms of arbitration are agreed upon. Parties may limit by contract the issues which can be arbitrated as well as specifying by contract the rules to use in arbitration.[8] The intent of the FAA is to ensure that agreements to arbitrate are carried out precisely according to their terms. It would be counter-productive to find an agreement unenforceable because it specifies that a different set of rules other than the FAA applies to the situation.

What the FAA does do is preempt inconsistent state law and govern all aspects of the arbitration procedure for cases that fall within its reach.[9] The Supremacy Clause of Article VI of the United States Constitution prevents

[5] *Stewart Title Guaranty Co. v. Mack*, 945 S.W.2d 330, 332 (Tex. App. 1997), *citing* *Cantella & Co. v. Goodwin*, 924 S.W.2d 943, 944 (Tex. 1996).
[6] *Albright v. Edward D. Jones & Co.*, 571 N.E.2d 1329, 1332-33 (Ind.Ct.App. 1991), *citing* *Volt Information Sciences Inc. v. Board of Trustees*, 489 U.S. 468 (1989).
[7] *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 56, *citing* *Southland*, 465 U.S., at 10.
[8] *Id.*, at 57, *citing* *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 628 (1985).
[9] *Aviall, Inc. v. Ryder System, Inc.*, 913 F.Supp. 826, 830 (S.D.N.Y. 1996).

states from enacting valid legislation that contradicts federal law and policy. State law, even if it is clearly within a State's acknowledged power, must yield if it interferes with or is contrary to federal law.[10] Preemption can be either express or implied, whether Congress's intentions are "…explicitly stated in the statute's language or implicitly contained in its structure and purpose."[11] State law may also be preempted to the extent that it conflicts with federal law. This is true where it "…stands as an obstacle to the full accomplishment and execution of the full purposes and objectives of Congress."[12] A contradiction between state and federal law is not always necessary to apply the parameters of the Supremacy Clause. It is sufficient that a state law is an obstacle to the achievement of the full purposes that Congress has set out to accomplish for application of the Supremacy Clause to begin.[13]

One of these purposes is to ensure that parties to a contract are bound to the terms of an arbitration agreement. Even if this agreement removes it from the purview of federal law and binds the parties under state law, it must stand under the intent of the FAA. The FAA does not apply to actions where the parties have provided for state choice-of-law in an agreement, even if interstate commerce is involved.[14] It is not entirely clear, however, if state choice-of-law will stand if in so doing the arbitration agreement is unenforceable. Different jurisdictions have split on this question.[15]

INTERSTATE COMMERCE

Contracts to arbitrate are to be upheld over any conflicts with state law because of the Supremacy Clause. In order for the FAA to prevail under this rule, however, the transaction must involve interstate commerce. By enacting the FAA, Congress withdrew the power of the states

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[10] *Gade v. National Solid Waste Management Ass'n*, 505 U.S. 88, 108 (1992).
[11] *Id.*, at 98.
[12] *Volt Information Sciences, Inc. v. Board of Trustees of Leland Stanford Junior Univ.*, 489 U.S. 468, 477 (1989), *quoting* *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941).
[13] *Securities Indus. Assoc. v. Connolly*, 883 F.2d 1114, 1118 (1st Cir. 1989).
[14] *Paul Davis Systems of Northern Illinois, Inc., an Illinois Corp. v. Paul W. Davis Systems, Inc, a Florida Corp..*, 1998 WL 749041 (N.D. Ill. 1998), *citing* *Yates v. Doctor's Associates*, 549 N.E.2d 1010, 1015 (Ill. App. Ct. 1990).
[15] See *Albright*, 571 N.E.2d 1329; *Paul Davis Systems*, 1998 WL 749041; *Roberson v. Money Tree of Alabama, Inc.*, 954 F.Supp. 1519 (M.D. Ala. 1997); *Howard Fields & Associates v. Grand Wailea Company*, 848 F.Supp. 890 (D. Haw. 1993).

to require a judicial forum for resolution of claims that the contracting parties agreed to resolve by arbitration.[16] Still, the "involving commerce" requirement of the FAA is a necessary qualification in a statute intended to apply in both state and federal courts.[17]

One of the primary purposes of the federal Act is to reduce the volume of litigation in our court systems. Congressional policy is that this reduction is to take place by the utilization of binding arbitration.[18] This goal would not be met if parties could move to a judicial forum at will, or choose a forum where state law limits the enforceability of arbitration agreements. Thus, Congress enacted a provision that reaches to the extent of its power to regulate commerce between the states and mandates the enforcement of arbitration agreements in federal and state courts where such transactions are involved. It is clear then, that a finding of interstate commerce is a necessary component to begin application of the federal act and preemption of any state laws that limit the use of arbitration. The only limitations on the enforcement of arbitration provisions under the federal act is that they must be part of a written maritime contract or a contract evidencing a transaction involving interstate commerce.

The FAA is based on Congressional authority to enact substantive laws under the Commerce Clause.[19] The Supreme Court concluded that the statute "is based upon…the incontestable federal foundations of 'control over interstate commerce and over admiralty.'"[20] Once there is a transaction involving interstate commerce, federal substantive law begins to operate and will preempt any limitations imposed by state law. "[W]hen Congress exercises its authority to enact substantive federal law under the Commerce Clause, it normally creates rules that are enforceable in state as well as federal courts."[21] The Court has stated time and again that the FAA creates a body of federal substantive law that is applicable in both state and federal courts.[22]

The FAA is only applicable, however, if the contract evidences a transaction involving interstate or foreign commerce.[23] Without interstate commerce, there is no basis

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[16] *Southland*, 465 U.S. 1, 10.
[17] *Id.*
[18] *Id.*, at 7.
[19] *Prima Paint Corp. v. Flood & Conklin Manufacturing Corp.*, 388 U.S. 395 (1967).
[20] *Id.*, at 405.
[21] *Southland*, at 12, *citing* *Prima Paint*, at 420 (Black, J., dissenting).
[22] *Moses H. Cone Memorial Hospital v. Mercury Construction Corp*,
[23] *Varley v. Tarrytown Associates, Inc.*, 477 F.2d 208, 209 (2nd Cir. 1973).

for the FAA to apply, and state arbitration law must govern the contract or agreement in question.[24] Interstate commerce is a necessary base upon which the FAA is predicated. Courts continue to hold that in order for the FAA to become applicable there must be two findings:

1. That there was a written agreement providing for arbitration; and
2. That the contract evidences a transaction involving interstate commerce.[25]

TERMINIX

The leading case on arbitration from the United States Supreme Court is *Allied-Bruce Terminix Companies, Inc. v. Dobson*. In *Terminix*[26], the Court held that the FAA preempts state law making pre-dispute arbitration agreements unenforceable. A dispute between an extermination company and homeowners over the performance of an extermination contract led to the homeowners filing suit against the company. The company then sought a stay invoking the arbitration clause in the agreement. The Alabama Supreme Court upheld the denial of the stay based on Alabama law making pre-dispute arbitration agreements unenforceable.

The United States Supreme Court reversed the Alabama Supreme Court by determining that the FAA's interstate commerce language should be read broadly to extend the Act's reach to the limits of Congress's Commerce Clause power. The Court reasoned that the legal background of the FAA demonstrates that its purpose is to overcome state courts' refusals to enforce agreements to arbitrate. Permitting Alabama to apply its anti-arbitration statute would be inappropriate because the Court previously decided that "Congress would not have wanted state and federal courts to reach different outcomes about the validity of arbitration in similar cases".[27] The conclusion is that the FAA preempts state law, therefore state courts cannot apply state statutes that invalidate arbitration agreements per

[24] *Shearson Hayden Stone, Inc.*, 493 F.Supp. 104, 106 (N.D. Ill. 1980), *citing* *Pawgan v. Silverstein*, 265 F.Supp. 898, 901 (S.D.N.Y. 1967).
[25] *American Home Assurance Co. v. Mercury Construction Corp.*, 629 F.2d 961, 963 (4th Cir. 1980), *citing* *Bernhardt v. Polygraphic Co.*, 350 U.S. 198 (1956).
[26] 513 U.S. 265 (1995).
[27] *Id.*, at 272, *citing* *Southland Corp. v. Keating*, 465 U.S. 1 (1984).

se if there is a transaction involving interstate commerce.[28]

The FAA provides in part that "…a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction…shall be…enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."[29] The Court held that the word "involving" is the functional equivalent of "affecting" for the purposes of this statute and points to a significant congressional intent: "That phrase—'affecting commerce'—normally signals a congressional intent to exercise its Commerce Clause powers to the full."[30] This broad interpretation is consistent with the FAA's basic purpose of making arbitration agreements equal to other terms of a contract.[31]

The Court concluded that in order to further this intent the "commerce in fact" interpretation would more accurately fit the intent of the statute than the "contemplation of the parties" interpretation.[32] "Commerce in fact" means that the transaction must turn out, in fact, to have involved interstate commerce. "Contemplation of the parties", however, questions whether at the time parties enter into and accept an arbitration clause they contemplate substantial interstate activity. In deciding against the latter approach, the Court reasoned, "Why would Congress intend a test that risks the very kind of costs and delay through litigation (about the circumstances of contract formation) that Congress wrote the Act to help the parties avoid?"[33]

Finally, the Court set out in clear terms what States could and could not do in attempting to protect consumers against unfair arbitration provisions. Section 2 of the FAA gives States a valid method, "…upon such grounds as exist at law or in equity for the revocation of any contract."[34] What they may not do is, "…decide that a contract is fair enough to enforce all its basic terms (price service, credit), but not fair enough to enforce its arbitration clause. The Act makes any such state policy unlawful, for that kind of policy would place arbitration clauses on an unequal 'footing,' directly contrary to the

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[28] *Id.*
[29] 9 U.S.C. § 2.
[30] *Terminix*, at 273, *citing* *Russell v. United States*, 471 U.S. 858, 859 (1985).
[31] *Id.*, at 274, *citing* *Scherk v. Alberto-Culver Co.*, 417 U.S. 506, 511 (1974).
[32] *Id.*, at 278.
[33] *Id.*
[34] 9 U.S.C. § 2.

Act's language and Congress's intent."[35] Therefore, any state law setting apart arbitration agreements for treatment different from other contract terms in general will not pass muster if the transaction involved interstate commerce in fact, regardless of whether or not the parties contemplated an interstate transaction.

CONTRACT DEFENSES

The FAA itself lists certain grounds for a court to vacate an arbitration award. These include instances "where the award was procured by corruption, fraud, or undue means."[36] The ability of a court to vacate arbitration awards is, for the most part limited by the FAA to the reasons set forth in the Act. There must be "…some causal relation between the undue means and the arbitration award".[37] In order to vacate an award under these grounds the claimant must offer proof that the conduct in question caused the procural of the award by undue means. Arbitration might be challenged, however, before the process ever reaches the award stage.

One of the possible, successful challenges to enforcement of an arbitration clause is a general contract defense such as unconscionability, fraud, or duress. Even if the clause falls under the FAA, the statute makes it clear that defenses applying to contracts generally are an exception to the federal presumption in favor of arbitration.[38] The United States Supreme Court stated, "[T]he text of §2 declares that state law may be applied 'if that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally.' Thus, generally applicable contract defenses, such as fraud, duress, or unconscionability, may be applied to invalidate arbitration agreements without contravening §2."[39]

It is important to note, however, that the arbitration clause itself must be unenforceable and not some other term of the contract. If the arbitration clause passes muster then it is possible the arbitrator will have jurisdiction over the rest of the contract along with the ability to determine the validity of other terms. In order for a

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[35] *Terminix*, at 281.
[36] 9 U.S.C.A. §10(a)(1)
[37] *Painewebber Group, Inc. v. Zinsmeyer Trusts Partnership*, 1999 WL 238453 (8th Cir. 1999).
[38] 9 U.S.C.A. §2
[39] *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681, 686 (1996).

court to have jurisdiction, it is not the overall contract that must be in dispute. There must be a question as to whether the arbitration clause is binding. Any disputes over the remainder of the contract will be made by the arbitrator.[40] The arbitration clause itself can questioned if a party is forced to arbitrate whether he had been pressured or tricked into agreeing to arbitrate in the first place.[41]

For example, an Indiana court found that when a broker knowingly misstates a writing's contents in order to induce a client to sign, it is unenforceable as fraudulent. More specifically, it is fraud in the inducement of the contract. The contract in question is then revocable under Indiana law, and falls within the exception contained in both the federal and state arbitration acts on grounds "existing at law or in equity for the revocation of any contract."[42] If the writing in question is an arbitration clause, it is unenforceable.

Generally speaking, to find unconscionability there must be some showing of an absence of a meaningful choice in agreeing to contract on the part of one of the parties together with contract terms unreasonably favorable to the other party. These two findings are sometimes referred to as procedural and substantive unconscionability, respectively. Procedural unconscionability refers to the circumstances under which the contract was negotiated and signed. Substantive unconscionability refers to the content of the contract. These are conjunctive elements of an unconscionability claim under Indiana law and both must be found to support such a claim.[43]

A party seeking to enforce an unconscionable contract has the burden of proving that the provisions were explained to the other party and came to their knowledge, and that there was a real and voluntary meeting of the minds rather than merely an objective one. The Indiana Supreme Court has held that when a party can show that a contract sought to be enforced is in fact an unconscionable one, the contract provision, or the contract as a whole if the provision is not separable, should not be enforced because it is contrary to public policy.[44]

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[40] *Matterhorn, Inc. v. NCR Corporation*, 763 F.2d 866, 869 (7th Cir. 1985), *citing* *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402, 410-11 (2nd Cir. 1959), *cert. Dismissed*, 364 U.S. 801, 81 (1960).
[41] *Id.*
[42] *A.G. Edwards and Sons, Inc. v. Hilligoss*, 597 N.E.2d 1, 3 (Ind. Ct. App. 1991), *quoting* 9 U.S.C.A. §2, IC 34-4-2-1.
[43] *Comunications Maintenance, Inc. v. Motorola, Inc.*, 761 F.2d 12002 (C.A.7 (Ind.) 1985).
[44] *Weaver v. American Oil Col.*, 276 N.E.2d 144, 148 (Ind. 1971).

Inequality of bargaining power is not enough to invalidate a contract as one of adhesion. Furthermore, the fact that a consumer doesn't read an agreement or later claims not to have understood it does nothing to invalidate a contract either. However, a showing of a combination of an absence of meaningful choice together with unreasonably favorable contract terms taken together can demonstrate unconscionability to an extent that the contract will not be valid. Possible inconvenience alone may not rise to the level of unconscionability; however, an excessive cost factor that is necessarily entailed can be unreasonable and serve to deter the individual consumer.[45] Excessive fees have also been grounds for finding an arbitration clause unenforceable as being unconscionable.[46]

Lack of mutuality in and of itself does not render an arbitration clause unenforceable. As stated repeatedly, federal law presumptively favors the enforcement of arbitration agreements. However, generally applicable contract defenses may be applied without contravening the FAA.[47] A finding of unconscionability, for example, "…requires a two-fold determination: that the contractual terms are unreasonably favorable to the drafter and that there is no meaningful choice on the part of the other party regarding acceptance of the provisions."[48] Such a finding as it pertains to an arbitration clause is enough to make it unenforceable as being unconscionable.

WAIVER OF RIGHTS

A subject of particular interest is an arbitration clause which includes some waiver of rights by a signing party. Indiana's Uniform Consumer Credit Code (UCCC) includes a section on such a waiver which states, "Except as otherwise provided in this Article, a buyer, lessee, or debtor may not waive or agree to forego rights or benefits under this Article."[49] This differs from the Uniform Consumer Code (UCC), which broadly permits variation by agreement[50], in that the UCCC starts from the premise that a consumer generally may not waive their rights under this

[45] Brower v. Gateway 2000, Inc., 246 A.D.2d 246, 254 (N.Y. App. Div. 1998).
[46] Id., *citing* Matter of Teleserve Systems, 230 A.D.2d 585, 593-594 (N.Y. App. Div. 1997).
[47] Harris v. Green Tree Financial Corporation, 1999 WL 445642, 4 (3rd Cir. 1999), *citing* Doctor's Associates, Inc. v. Distajo, 66 F.3d 438, 451-53 (2nd Cir. 1995).
[48] Id. at 6, *citing* Bensalem Township v. International Surplus Lines Ins. Co., 38 F.3d 1303, 1312 (3d Cir. 1994), *quoting* Worldwide Underwriters Ins. Co. v. Brady, 973 F.2d 192, 196 (3rd Cir. 1992).
[49] IC 24-4.5-1-107(1).
[50] UCC Section 1-102(3).

Act. The UCCC further states that any settlement in which a debtor waives rights is invalid if the court finds it to have been unconscionable at the time it was made.[51] The combination of these subsections makes a significant difference in the analysis of arbitration clauses.

Two recent cases signal a shift in the way courts approach the validity of arbitration clauses by focusing on a waiver of rights. The first concerns arbitration agreements contained in employment agreements. In *Ramirez v. Circuit City Stores, Inc*[52], the California Court of Appeals found that an agreement which calls for final and binding arbitration in any disputes cannot be upheld where the plaintiff was given no choice but to sign the document, stating, "A meaningful choice requires more than the choice…between forgoing the possibility of employment or applying for a job but agreeing to what, superficially, appears to be a fair means of resolving employment disputes."[53]

The court used this as a basis for finding the agreement unenforceable because the limitations imposed by the arbitration agreement on class actions and on the rights and remedies of employees and prospective employees was unconscionable. The lack of meaningful choice would not be enough to render the agreement unenforceable if the terms of the agreement were fair. However, the court stated, ***"[It is] well-settled that an agreement that requires the weaker party to arbitrate any claims he or she may have, but permits the stronger party to seek redress through the courts, is presumptively unconscionable***."[54] *(emphasis added)*.

The court noted that limiting or eliminating the ability of an employee to obtain relief was previously condemned by the California Supreme Court.[55] The emphasis here was the importance of class actions as a means of vindicating rights asserted by large groups. The class action is meant to eliminate repetitious litigation and provide small claimants with a method to obtain relief for claims which would otherwise not warrant litigation because of the smaller amounts involved.[56] The elimination of the class action device would benefit the defendant and

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[51] IC 24-4.5-1-107(4).
[52] 1999 WL 1129013 (Cal.App. 1 Dist. 1999).
[53] *Id.*, at *3.
[54] *Id., citing Kinney v. United Healthcare Services, Inc., supra*, 83 Cal.Rptr.2d 348; *Stirlen v. Supercuts, Inc.*, 60 CalRptr.2d 138 (1997).
[55] *Keating v. Superior Court*, 645 P.2d 1192 (1982) (app. dism. In part and judg. revd. in part on other grounds sub. nom. *Southland Corp. v. Keating*, 465 U.S. 1 (1984).
[56] *Ramirez*, at *4, *quoting Keating*, at 1192.

disadvantage the affected members of the class. When a contract is one of adhesion, and terms of that contract prohibit implementation of the class action process, courts have held such a prohibition is ***not binding because it would effectively eliminate individual claims***.[57]

The same general reasoning led to identical results in *Johnson v. Tele-Cash, Inc.*[58], in a U.S. District Court ruling from Delaware. Here the court found a clear Congressional intent to preclude the arbitration of claims arising under the Truth in Lending Act (TILA) by explicitly allowing for the possibility of class relief under the statute.[59] If the court were to compel arbitration in such a case, "…the federal statute would be effectively stripped of its 'sting' and reduced to nothing more than its mere 'nuisance' value."[60] In other words, removing the supposed "right" to take advantage of class relief would frustrate the intent of the TILA, making it questionable that the act could continue to serve its remedial and deterrent function.[61] The court did, however, grant a motion to dismiss as it related to the claim that the arbitration clause in questions was itself unconscionable since its terms were not so one-sided as to be oppressive.

It is important to note that in this case the court did not find a right to class relief. The holding makes it clear that arbitration could not be compelled because of the Congressional intent to allow class relief for TILA violations. As such, the waiver of class relief contained in the arbitration clause was at odds with a federal statute designed for a remedial and deterrent function. If TILA had not been an issue here, the waiver of rights would not be enough to find the arbitration clause unenforceable.

Using these two cases as a starting point, recent case law tends to lean towards the same analysis. Namely, if a party has been forced to waive certain rights by signing an adhesion contract that contains a binding arbitration clause then courts will carefully scrutinize the terms in order to determine if the clause is unconscionable as a matter of law. The involvement of a waiver of rights subjects the arbitration clause to a high level of scrutiny as to whether or not it is unconscionable. A finding of unconscionability leads to an unenforceable arbitration

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[57] *Id.*
[58] 82 F.Supp.2d 624 (D.Del. 1999).
[59] *Id.*, at 268.
[60] *Id.*, at 270, citing *Bantolina v. Aloha Motors, Inc.*, 419 F.Supp. 1116, 1120 (D.Haw. 1976).
[61] *Id.*, citing *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 637 (1985).

clause if it is contained in a contract of adhesion. Indiana law specifically mandates this outcome in the UCCC.

Nonetheless, this question has yet to be settled. The U.S. Supreme Court recently agreed to review a case out of the 11th Circuit which barred the invocation of an arbitration clause because it failed to provide minimum guarantees required for the plaintiff to vindicate her statutory rights.[62] The appellants contend that this decision violates the requirement that a reviewing court should resolve doubts about the arbitratability of statutory claims in favor of arbitration. Until the Court answers this question definitively there will continue to be a split between different Circuits. The 7th Circuit, which includes Indiana, has not decided this issue either way.

CONCLUSION

The enforceability of arbitration clauses in Indiana is not a foregone conclusion. It will depend mostly on two different determinations. The first is whether the contract involves interstate or intrastate commerce. If interstate, the FAA applies and arbitration clauses cannot be held to standards different from those applicable to contracts generally. If intrastate, then Indiana law applies and arbitration clauses in loan contracts are invalid. There is no true consensus, however, on how state or federal law should be applied to arbitration clauses. The U.S. Supreme Court will have to make a ruling on the split decisions between Circuits that currently exists on different questions. Until then, it falls upon the Department to make a determination as to how arbitration clauses will be judged in the State of Indiana.

Since most loan contracts will be able to fall under the ambit of interstate commerce, thus precluding Indiana law with the federal act, the second determination regarding arbitration clauses becomes the most important. If defenses available to contracts in general can be applied to the arbitration clause as well, its enforceability becomes an issue. In particular, a clause that contains terms which are unconscionable, oppressive, or completely one-sided is contrary to public policy and should be unenforceable.

[62] *Randolph v. Green Tree Fin. Corp.*, 178 F.3d 1149 (11th Cir. 1999).

Since most, if not all, transactions in this area will be able to demonstrate some relationship to interstate commerce, a prudent response from a policy standpoint is to treat all loan contracts as transactions involving interstate commerce. Consequently, the Department will not have to scrutinize every agreement containing an arbitration clause to determine whether or not it truly involves interstate commerce. Indiana statutes and the case law surrounding arbitration provide ample legal grounds to find arbitration clauses unenforceable when they are used to take advantage of unsuspecting consumers. If these clauses are all treated as falling under the FAA, even in cases where it would not be necessary, there will be no issues arising regarding a preemption of state law.

The Department would be well-advised to take whatever actions necessary in these cases to ensure arbitration clauses are not inserted into consumer credit contracts in an attempt to take advantage of unwary or unsophisticated consumers. In addition, where federal statutes such as TILA are concerned the Department has a duty to ensure that the remedial and deterrent effects are not gutted by arbitration clauses which remove the option of class relief. The same holds true for state statutes governing the waver of rights by a debtor. Where the General Assembly has expressed the legislative intent to guard consumers from unconscionable terms, the Department’s policy should be to follow this directive as prudently as possible.